
Bryan J. Leary

Thomas G. Wallrich

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COMMENTS

THE NIGHT BEFORE BANKRUPTCY: THE EIGHTH CIRCUIT'S RESPONSE TO BANKRUPTCY ESTATE PLANNING

[Norwest Bank Nebraska v. Tveten, 848 F.2d 871 (8th Cir. 1988) and Panuska v. Johnson (In re Johnson), 80 Bankr. 953 (Bankr. D. Minn. 1987)]

INTRODUCTION

'Twas the night before bankruptcy and all through the house, not a debtor was earning, not even a spouse. Exemptions were picked by attorneys with care, in hopes that debt discharge soon would be there. The creditors lay sleeping all snug in their beds, while fraudulent transfers danced in their heads. Being empty of head, but pure in my heart, I had just settled down to enjoy my "fresh start."

Wanting to preserve as much of one's property in spite of bankruptcy is a natural human desire—^the instinct for self-preservation. The conversion of nonexempt assets into exempt assets is thus an understandable temptation for any debtor contemplating bankruptcy. Temptation or not, the appropriateness and legality of such conversions presents a perplexing and unresolved question: Is it lawful bankruptcy estate planning or an unlawful effort to thwart creditors? As one might expect, the answer ultimately depends on who is asked and on which side of the issue they stand. On one side, creditors argue that such conversions are a depletion of assets available for distribution to creditors. On the other side, debtors maintain that it is merely an exercise of the debtor's rights under existing bankruptcy law. Within the penumbra of uncertainty that surrounds

2. For purposes of this Comment, the term "bankruptcy estate planning," refers to conduct by debtors undertaken to increase the amount of assets retained by the debtor and to reduce the extent of his liabilities after bankruptcy. This includes the conversion of nonexempt, unsecured assets into exempt assets within one year prior to the filing of bankruptcy. Transfers occurring more than one year before filing bankruptcy are scrutinized under a common law fraud analysis. The term "bankruptcy estate planning" is to be distinguished from the general term "prebankruptcy planning" which, though including those aspects, incorporates other conduct such as a debtor's attempts to maintain relationships and favor certain creditors. See Nimmer, Consumer Bankruptcy Abuse, 50 LAW & CONTEMP. PROBS. No. 2, 89, 100-09 (1987).

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the issue, bankruptcy judges are forced to choose between two extremes. The polarity of current opinion is exemplified in the recent cases of Norwest Bank Nebraska v. Tveten and Panuska v. Johnson.

Tveten and Johnson are two more in a line of cases striving to distinguish between transfers that are the proper exercise of exemption rights and transfers made with the intent to hinder, delay, or defraud creditors. In both cases, the property conversions were initiated as part of each debtor's overall bankruptcy estate planning. In Tveten, the Eighth Circuit Court of Appeals affirmed the bankruptcy court's findings of intent to hinder, delay, or defraud creditors in connection with the debtor's conversion of approximately $700,000 of nonexempt assets into exempt assets. This decision, however, sows uncertainty for debtors considering bankruptcy because the court failed to articulate a clear standard as to what constitutes wrongful bankruptcy estate planning.

Similar facts, yet differing results, make Tveten and Johnson difficult cases to reconcile. This difficulty is compounded in that both cases arise in the same bankruptcy district, review similar debtor conduct, and interpret the same controlling statute. In addition, the debtors in both cases were business associates, represented by the same legal counsel, and sought discharge of the same debts. In Johnson, the conversion of approximately $435,000 worth of nonexempt property to exempt property was seen as mere "bankruptcy estate planning" which did not warrant a denial of discharge.

The issue raised in both Tveten and Johnson strikes at the very core of bankruptcy law. To analyze this issue, the fundamental aspects of the controversy must be considered in light of the overall aim and purpose of bankruptcy in our society. This Comment will first examine the development and policy considerations of the discharge and exemption provisions in bankruptcy and the judicial analysis of bankruptcy estate planning. This Comment will then examine the

3. 848 F.2d 871 (8th Cir. 1988).
6. Tveten, 848 F.2d at 876-77. Not only was the debtor denied discharge, but his claimed exemptions were also lost. The bankruptcy court raised a question as to the validity of the exemptions under Minnesota law. The Minnesota Supreme Court, in response to the questions certified by the bankruptcy court, held that the state statute granting the claimed exemption violated the Minnesota Constitution and was therefore invalid. See In re Tveten, 402 N.W.2d 551 (Minn. 1987).
reasoning underlying the *Tveten* and *Johnson* holdings and the impact of these two cases on bankruptcy estate planning.

I. DEVELOPMENT AND POLICY CONSIDERATIONS OF THE DISCHARGE AND FRESH START PROVISIONS IN BANKRUPTCY

By converting nonexempt property into exempt property, bankruptcy estate planning places the policies of discharge of debts and exemptions of property in a struggle for supremacy. While theoretically separate and distinct, the policies advanced by these two aspects of bankruptcy law promote related interests within the Bankruptcy Code.

A. Discharge of Debts in Bankruptcy

1. Development of Discharge in Bankruptcy

Discharge from debts is the obvious and ultimate goal of an individual debtor under current bankruptcy law. When it is granted, discharge not only frees the debtor from personal obligations owed to his creditors, but it permanently enjoins creditors from collecting prebankruptcy debts or recovering from the debtor's postbankruptcy earnings or property. Through discharge the debtor receives a clean economic slate.

As common as discharge has become, it has not always been so liberal or available. Despite biblical directives to the contrary, early bankruptcy laws did not discharge a debtor from the obligations owed to his creditors. Instead, there existed quasi-punitive

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8. The term “discharge” has held a variety of meanings in connection with bankruptcy law. Previously, the term has included payment of the debt, release from liability for arrest and suit, or release from debtor’s prison. In current bankruptcy lexicon, the word “discharge” applies to the debtor’s release from liability for debts. See Ayer, infra note 13, at 367 n.40.

9. See B. WEINTRAUB & A. RESNICK, supra note 1, at § 1.02 n.2.

10. 11 U.S.C. § 524 (1982 & Supp. IV 1986). The granting of discharge has the effect of voiding any judgment pertaining to a discharged debt, enjoining the commencement, continuation, or issue of legal process to recover or collect any such debt as a personal liability of the debtor or against property acquired by the debtor after the commencement of the case. Id.

11. At the end of every seven-year period you shall have a relaxation of debts, which shall be observed as follows. Every creditor shall relax his claim on what he has loaned his neighbor; he must not press his neighbor, his kinsman, because a relaxation in honor of the Lord has been proclaimed. You may press a foreigner, but you shall relax the claim on your kinsman for what is yours. Deuteronomy 15:1-4.

12. The early English system of bankruptcy evolved from a crude form of bankruptcy liquidation created under Roman Law as far back as 118 B.C. Under the Roman law, a debtor’s estate was sold in a lump sale to a buyer who would pay the creditors a percentage of the debt. Since a debtor was liable for his debts with his life
measures aimed at punishing the debtor's perceived active wrongdoing in not paying his debts. The modern concept of debt discharge did not appear in statutory form until the early eighteenth century under the reign of Queen Anne of England.

In the United States, discharge has been a feature of American bankruptcy law since its inception. The first American bankruptcy law provided for a limited discharge, but the approval of two-thirds of the creditors was required. The second Bankruptcy Act, adopted in 1841, departed from the previous Act and granted discharge unless the creditors objected. The economic crisis following the Civil War produced the third Bankruptcy Act, which further liberalized the granting of discharge. From that point, it was a short step to the absolute discharge provided in the Bankruptcy Act of 1898.

The original purpose prompting discharge provisions was not, as and body, no discharge was granted. See Countryman, A History of American Bankruptcy, 81 Com. L.J. 226, 226 (1976).

13. While debtor dissection and debtor slavery were not sanctioned by English law, procedures developed whereby a creditor could have a debtor imprisoned and held until the debt was paid. Id. (citing Statute of Acton Burnell, 11 Edw. I (1283); Statute of Merchants, 13 Edw. I, Stat. 3 (1285)).

Enacted in 1542, the first English bankruptcy law only served to enlarge prison populations. The law applied to those persons "craftily obtaining into their hands great substance of other men's goods, who suddenly flee to parts unknown or keep their houses, not minding to pay or restore to their creditors their debts and duties, but at their own will and pleasure consume the substance obtained by credit of other men, for their own pleasure and delicate living against all reason, equity and good conscience." See Ayer, How to Think about Bankruptcy Ethics, 60 Am. Bankr. L.J. 355, 367 n.39 (1986).


Not all debtors were eligible for bankruptcy, but for those who were, the Act provided complete relief. . . . It discharged all debts existing when the proceeding was commenced and was available over the objections of creditors. . . . In 1706, Parliament instituted the requirement that four-fifths of debtors' creditors, in number and amount, must consent to the granting of discharge.

Id. (citing An Act to Explain and Amend an Act of the Last Session of Parliament for Preventing Frauds Frequently Committed by Bankruptcy, 6 Anne, ch. 22, § 2 (1706)).


17. This Act provided that a debtor paying his creditors at least fifty percent of his debt need not obtain a favorable vote from his creditors. This percentage was later reduced to thirty percent by an amendment added in 1874. Bankruptcy Act of 1867, ch. 176, § 33, 14 Stat. 517, amended by, Act of Jun. 22, 1874, ch. 390, § 9, 18 Stat. 178, (repealed 1878). See Countryman, supra note 12, at 229.

one might suppose, a benevolent endeavor to relieve the debtor's economic woes.19 Discharge was initially offered as an inducement to gain the debtor's cooperation in the bankruptcy proceedings.20 The debtor was considered more likely to cooperate with the proceedings if rewarded for his involvement. Today, debtor cooperation is encouraged by the explicit punishments for the debtor's failure to assist in the proceedings.21 The advent of the "fresh start" policy, with the enactment of the Bankruptcy Act of 189822 ushered in a new age of bankruptcy theory.

2. The Fresh Start Policy

The fresh start policy changed the purpose of discharge and with it the entire focus of the bankruptcy process.23 With the discharge provisions at its heart,24 the fresh start policy is laden with humanitarian25 and paternalistic26 concerns independent of the creditor-

19. Ayer, supra note 13, at 368.
20. J. MacLachlan, Handbook of the Law of Bankruptcy, 20–21 (1956). The early English discharge provisions were introduced "not primarily, it would appear, out of consideration for the debtor's hardship. Penal sanctions had not evoked satisfactory cooperation from debtors directed to surrender their estates for administration by bankruptcy courts. The discharge was promoted as a reward for debtors who gave better cooperation." Id.; see also Ayer, supra note 13, at 368 n.45 (citing 4 Anne ch. 17 (1705)).
21. A debtor may be denied discharge for failing to cooperate with the bankruptcy proceedings. See 11 U.S.C. § 727(a)(4)-(6) (1982) (denial of discharge for making false oath; false claim; withholding information or records from the trustee; failure to explain satisfactorily any loss of assets or deficiency of assets to meet debtor's liabilities; refusing to obey orders of the court).
23. See Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) (the fresh start is supposed to give the honest but unfortunate debtor a new opportunity in life and a clear field for future effort); Williams v. United States Fidelity & Guar. Co., 236 U.S. 549, 554-55 (1915) (to relieve the honest debtor from the weight of oppressive indebtedness and permit him to start afresh). In examining the legislative intent behind the passage of the 1898 Act, it is apparent that Congress viewed the fresh start policy as beneficial to society as a whole. Ayer, supra note 13, at 368. In passing the 1898 Act, Congress stated:

The friends of a bankruptcy law contend that when an honest man is hopelessly down financially, nothing is gained for the public by keeping him down, but, on the contrary, the public good will be promoted by having his assets distributed ratably as far as they will go among his creditors and letting him start anew. The recent financial crisis has crippled so many good, aggressive, useful citizens all over the country that present conditions appeal loudly for the passage of a bankruptcy law.

25. The humanitarianism embodied by the fresh start policy is reflected by the expression that discharge is directed toward "reliev[ing] the honest debtor from the weight of oppressive indebtedness and permit[ing] him to start afresh from the obligations and responsibilities consequent upon business misfortunes." The case cus-
oriented distribution rules of bankruptcy law. It appears that creditor collection efforts have taken a back seat to the debtor's financial rehabilitation.27

The fresh start discharge enables individuals to preserve future earnings, for future consumption, free from past debts.28 Requiring a preservation of assets for the future serves societal as well as individual interests by fostering renewed productivity.29 The pressure of excessive debt on one's family, emotional health, and job security often seriously impair the debtor's productivity. In these cases a net social gain is realized by terminating costly collection efforts, excusing debts, and allowing the debtor a fresh start.30 The specific scope of that fresh start, however, remains unsettled. Whereas the overall purpose of the bankruptcy system is to promote the economic independence of productive persons, rather than the economic dependence of the destitute,31 it follows that the scope of fresh start, facilitated by discharge, should advance this goal.

3. Denial of Discharge

Emphasis on the interrelationship between discharge and fresh start policy can be misleading. Despite popular belief and catachresis, debt discharge is not a right.32 Discharge may be denied to punish those debtors engaging in conduct repugnant to the Bankruptcy

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26. The paternalistic aspect is illustrated in a number of ways, the least of which is that discharge is granted regardless of the cause of the debtor's financial misfortune. The shameless as well as unfortunate are entitled to discharge. Furthermore, discharge is nonwaivable right, and contracts that impair the right to file bankruptcy are unenforceable. Ayer, supra note 13, at 368-69.


28. See Jackson, The Fresh-Start Policy in Bankruptcy Law, 98 HARV. L. REV. 1393, 1398 (1985). Professor Jackson notes that the fresh start policy is largely limited to the protection of human capital as it manifests itself in earnings. Id.


31. See Howard, supra note 29, at 1079.

32. See United States v. Kras, 409 U.S. 434, 446 (1973) ("There is no constitutional right to obtain a discharge of one's debts in bankruptcy."); In re Tabibian, 289 F.2d 793, 795 (2d Cir. 1961) ("It is true that a discharge is a privilege granted the honest debtor and not a right accorded all bankrupts.").
The punitive character of this sanction is obvious. When discharge is denied all obligations owed to creditors remain intact and enforceable against the debtor at the close of the bankruptcy case. This also serves to deter certain wrongful conduct. Furthermore, denying discharge to debtors guilty of certain transgressions comports with the insistence of courts and commentators alike that only "honest but unfortunate" debtors receive the benefit of discharge.

When an objection to discharge is raised, it presents what is thought to be "one of the gravest possible issues" in a bankruptcy case. The objecting party or creditor must marshall compelling evidence of the debtor's violative conduct to support the denial. The type of conduct warranting denial of discharge has been described as the "broad, deliberate failure on the debtor's part to act fairly, equitably, and responsibly in the conduct of debtor-creditor relations." In the proscribed conduct warranting a denial of discharge, a common denominator can be seen. Each activity involves fraud or similar wrongdoing by the debtor aimed at foiling creditor collection efforts. Where the debtor has transferred assets on the eve of bankruptcy, the denial of discharge, as opposed to the recapture of assets, is considered an appropriate response, since all creditors suffer injury. Denial of discharge is not, however, the only avenue of attacking bankruptcy estate planning.

35. Jackson, supra note 28, at 1440.
38. Id.
39. Id.
40. A debtor may be denied discharge for making a false oath, using or presenting a false claim, withholding property from the estate, transferring property from the estate, failing to account for loss of assets, failing to obey an order of the bankruptcy court, concealing or destroying property. See 11 U.S.C. § 727(a) (1982 & Supp. IV 1986).
41. See Jackson, supra note 28, at 1446. This is to be compared with debts excepted from discharge under section 523. Under that section, a debtor will be denied discharge of a particular debt for the willful and malicious injury to another. The general difference between section 523 and section 727 has to do with the extent of the harm the activities cause. Injury occasioned by violation of section 727 is not directed toward a particular creditor as in the case of section 523. Jackson, supra note 28, at 1446 n.167.
42. A creditor or trustee challenging a conversion of nonexempt property to exempt property may do so under a number of legal theories. The conversion and claimed exemption may be challenged as fraudulent transfer under state or federal law. See 11 U.S.C. §§ 544(b), 548(a)(2) (1982 & Supp. IV 1986). It also may be chal-
Exemption provisions protect and provide for the debtor's fundamental human needs by limiting the assets available for distribution to creditors. Although exemption provisions have been part of American bankruptcy law from its inception, the common law had no regard for the plight of debtors or their families. Existing exemptions were based upon the purely practical consideration of what was needed to earn a living to repay debts. While the factors influencing individual state exemption law are varied, this austere trend was embraced in the northeastern United States.

The early federal bankruptcy laws contained their own exemptions independent of state exemption laws. As the economic fluctuations during the eighteenth and nineteenth centuries demonstrated, anyone could suffer from the economic uncertainties of modern society. Consequently, more generous exemption rights were approved to protect the populace from poverty. In 1867, a uniform
federal exemption was established giving debtors a choice between state and federal exemptions.\(^{51}\) However, this choice was eliminated in the Bankruptcy Act of 1898 which simply incorporated the exemptions of the debtor’s home state.\(^{52}\)

Under current bankruptcy law, all of the debtor’s property automatically becomes the property of the bankruptcy estate upon filing for relief.\(^{53}\) However, the debtor is allowed to claim certain property as exempt, thereby removing it from the bankruptcy estate and the reach of creditors.\(^{54}\) Under section 522 of the Bankruptcy Code, federal bankruptcy law incorporates state law by allowing debtors, in some cases, to choose between exemptions available under state law or those offered in the Bankruptcy Code.\(^{55}\) Although uniform federal exemptions were recommended,\(^{56}\) Congress enacted federal exemptions yet allowed states the power to limit residents to the exemptions available under state law.\(^{57}\) This compromise was designed to minimize the potential conflict between the federal and state exemptions.

Unless a state exercises its right to opt out,\(^{58}\) federal exemptions provide both a maximum dollar limitation as well as a minimum exemption level to protect those debtors in states with less generous exemption statutes.\(^{59}\) For the most part, property exempted under state law encompasses those things necessary for sustenance. Wearing apparel, cooking utensils, and bedding are common exemptions.\(^{60}\)

\(^{415, 417}\) (1941). In Poznanovic the Minnesota Supreme Court endorsed these principles by stating, “The humane and enlightened purpose of an exemption is to protect a debtor and his family against absolute want by allowing them out of his property some reasonable means of support and education and the maintenance of the decencies and proprieties of life.” \textit{Id.}


\(^{52}\) Bankruptcy Act of 1898, ch. 541, § 6, 30 Stat. 544, 548 (1898).


\(^{55}\) See 11 U.S.C. § 522(b) (1982 & Supp. IV 1986) (containing language allowing states to opt-out of the federal exemption and limit residents to the exemptions available under that state’s exemption laws).


\(^{58}\) See 3 Collier on Bankruptcy (MB) ¶ 522.02 n.4a (15th ed. 1989). Thirty-six states have enacted legislation opting-out of the federal exemptions and limiting debtor’s to exemptions available under state law. \textit{Id.}


2. The Exemption Policy

By allowing the retention of exempt property for use in the postbankruptcy period,\(^61\) exemption laws work in tandem with debt discharge in promoting the debtor's fresh start.\(^62\) In doing this, both state and federal exemption laws serve three related purposes essential to the fresh start policy: protecting the debtor from impoverishment during periods of financial stress, enhancing the debtor's prospects of future economic independence through rehabilitation, and placing the burden of credit-related social welfare problems on the creditor rather than society.\(^63\) Exemptions provide the resources with which the debtor can rehabilitate himself. If exemptions were not granted, the responsibility of supporting debtors through welfare payments would rest on society.\(^64\) A debtor seeking to shelter wealth through bankruptcy by converting it into exempt assets does not advance these purposes.\(^65\) Exemptions were neither created nor intended to benefit the dishonest debtor in perpetrating a fraud upon creditors.\(^66\)

From an economic standpoint, allowing the debtor to choose which property to claim as an exemption promotes the basic fresh start philosophy in a number of ways.\(^67\) By exempting property, the dual hardship that the debtor never anticipated the loss of the property and that the property which otherwise would be surrendered is more valuable to the debtor than to his creditors is alleviated.\(^68\) These hardships are minimized because allowing the debtor to select the assets which will be exempt protects the debtor from excessive "asset-loss" costs.\(^69\) Additionally, exemptions mitigate the effect of externalities\(^70\) caused by the debtor's "mortgaging" the future value

\(^{62}\) Howard, supra note 29, at 1077.
\(^{64}\) Resnick, supra note 47, at 626.
\(^{65}\) Jackson, supra note 28, at 1434.
\(^{66}\) Resnick, supra note 47, at 629.
\(^{67}\) Jackson, supra note 28, at 1439.
\(^{68}\) If a debtor were forced to surrender such property, the debtor would bear the cost of the difference between the present depreciated market value of the personal property and the value of his future consumption which is in excess of the property's present depreciated value. Id. at 1444.
\(^{69}\) Id. at 1427. "Asset-loss" cost is the additional cost in non-cash terms that the debtor bears when the asset is worth more to the individual debtor than it is to the creditors. Id.
\(^{70}\) Simply put, in the context of bankruptcy an externality is the cost borne by a
of property for present consumption. In choosing exemptions of the highest future value, a debtor decreases the probability of having to invest a greater amount of future earnings to repurchase that property, or passing the reacquisition cost to society. Most importantly, the exemption of wage substitutes, such as IRA's or whole life insurance contracts, preserves and supplements the debtor's future earnings and decreases the probability that the debtor will generate externalities.

While exemptions promote valid public policies, they have often been the target of criticism. Some state exemption statutes contain anachronistic provisions virtually unchanged since their enactment. What was undoubtedly a generous statute in the nineteenth century stands as a quaint relic in economic times. Similarly, some third party as a result of the debtor's conduct which is disproportionate to the cost borne by the debtor himself. Jackson, supra note 28, at 1418. An example of an externality that inflicts high costs on the debtor's family and society in general is the loss of the debtor's homestead. See, e.g., First Texas Sav. Ass'n v. Reed (In re Reed), 700 F.2d 986 (5th Cir. 1983).

71. Jackson, supra note 28, at 1419.
72. Id. at 1439 (debtors often exempt durable goods and wage substitutes thereby obtaining a fresh start without passing the cost of future consumption on to society).
73. See, e.g., Jackson, supra note 28, at 1434. Wage substitutes are defined as a form of savings, held by the debtor for use at a later time in lieu of wages. Such wage substitutes include annuitites or qualified pension plans. Id. The status of certain wage substitutes as an allowable exemption remains an issue, at least in the Minnesota bankruptcy district. In In re Netz, No. 3-88-1888 (Bankr. D. Minn. filed Oct. 17, 1988), the Minnesota bankruptcy court declared unconstitutional Minnesota's employee benefits exemption set forth in Minnesota Statutes section 550.37, subd. 24 (1988).
74. Jackson, supra note 28, at 1434.
75. See Countryman, Consumer Bankruptcy—Some Recent Changes and Some Proposals, 19 U. Kan. L. Rev. 165, 167 (1971); See also Joslin, Debtor's Exemption Laws: Time for Modernization, 34 Ind. L.J. 955, 375 (1959) ("nearly every jurisdiction is long overdue for a re-evaluation and analysis of its exemption laws. . . . It is evident that there is an urgency for a modernization of exemption laws, an urgency singularly and forcefully shown by even a casual observation of the archaic provisions and values still extant in the laws of most jurisdictions.").
76. In South Dakota, a debtor may exempt the following: two cows, five swine, two yoke of oxen, or one span of horses or mules, twenty-five sheep and their lambs under six months old, and all wool of the same, and all cloth and yarn manufactured therefrom, the necessary food for the animals hereinbefore mentioned for one year, either provided or growing, or both, as the debtor may choose; also one wagon, one sleigh, two plows, one harrow, and farming machinery and utensils, including tackle for teams, not exceeding twelve hundred fifty dollars in value. S.D. Codified Laws Ann. § 43-45-5 (1983). Under North Dakota law, a debtor may exempt "[a]ll crops and grain, both threshed and unthreshed, raised by the debtor on not to exceed one hundred sixty acres . . . of land in one tract occupied by the debtor, either as owner or tenant, as the debtor's home. . . ." N.D. Cent. Code § 28-22-02 (1987). A debtor may also exempt "[t]he provisions for the debtor and the debtor's
state exemptions are without dollar limitation.77

This economic and technological obsolescence coupled with the open-endedness of some state exemptions enables a debtor to keep property from creditors without serving a legitimate social policy objective.78 When this occurs, creditors are unduly hampered in the collection of their claims.79 The case of In re Freedlander80 reveals the inequity flowing from just such an exemption. In Freedlander, the debtor sought to exempt, pursuant to state exemption law,81 one thoroughbred race horse valued between $50,000 and $640,000.82 The creditors argued that to permit the debtor to retain such a valuable piece of property under the guise of exemption would subvert the spirit and purpose of the exemption.83 The bankruptcy court responded that, since the exemption statute antedated the advent of automobiles, the legislature probably only intended to allow debtors to retain some means of transportation.84 Nevertheless, the bankruptcy court declined to limit the exemption where the legislature had not.85 The bankruptcy court concluded that In re Maginnis86 supported the decision reached in Freedlander. In Maginnis, an exemption of $2,795 worth of china and silver was sustained pursuant to

family necessary for one year's supply, either provided or growing, or both, and fuel necessary for one year." Id.

77. A prime example of an open-ended exemption is the homestead exemption in Minnesota. Under Minnesota law, a house owned and occupied by a debtor as his dwelling place, together with the land upon which it is situated, constitutes the debtor's homestead and is exempt from seizure or sale under legal process. MINN. STAT. § 510.01 (1986). Furthermore, the family bible, library, as well as a seat in any house of worship and a burial lot are all exempted in an unlimited amount under Minnesota law. MINN. STAT. § 550.37, subd. 2, 3 (1986). But see In re Hilary, 76 Bankr. 683 (Bankr. D. Minn. 1987) (Kressel, J.) (holding that the unlimited exemption for musical instruments in MINN. STAT. § 550.37, subd. 2 is unconstitutional); In re Bailey, 84 Bankr. 608 (Bankr. D. Minn. 1988) (O'Brien, J.) (holding MINN. STAT. § 550.37, subd. 22 unconstitutional to the extent that those elements of a personal injury action constituting claims for special damages are exempted without limitation).

78. Resnick, supra note 47, at 628; Federal Policy, supra note 63, at 632.

79. Resnick, supra note 47, at 628.


81. "[E]very householder . . . shall . . . be entitled to hold exempt from levy or distress the following articles . . . to be selected by him . . . (5) . . . 1 horse." Id. at 450 (citing VA. CODE ANN. § 34-26 (1950)).

82. The horse was originally valued by the debtor at $650,000. However, the debtor, whose hobby was horse racing, maintained that the horse's poor showing in several races had considerably diminished the horse's value. Freedlander, 93 Bankr. at 450.

83. Id.

84. Id.

85. In 1876 the legislature removed a one hundred dollar limit on the value of an exemptable horse. Id. 450 n.2.

the same statute which also allowed a debtor to exempt six plates, twelve knives, twelve forks, two dozen spoon and twelve dishes.87 Conceding that the debtor in Freedlander was permitted more than the fresh start envisioned by the Bankruptcy Code, the bankruptcy court responded that, "if the law is in need of replacement or re-form, such action must issue from the legislature."88

II. Case Law Analysis of Bankruptcy Estate Planning

The bankruptcy system endeavors to reestablish the economic independence of the debtor. Essentially, this is accomplished by relieving the debtor from the weight of oppressive indebtedness and by making an equitable distribution of the debtor's nonexempt property to creditors.89 Although not mutually exclusive, these two aspects of the bankruptcy process are in constant tension. Neither an equitable distribution nor relief from indebtedness can be considered where the debtor has unlawfully depleted, through bankruptcy estate planning, the pool of assets available for distribution. The problem facing bankruptcy courts then is to avoid the unfair retention of assets by the debtor,90 while still advancing the fresh start policies underlying the discharge and exemptions statutes.

A. The Per Se Rule

The law is rife with cases involving debtors converting nonexempt property to exempt property in contemplation of bankruptcy.91 The

87. Freedlander, 93 Bankr. at 450.
88. Id. at 451.
91. Understanding how debtors approach the day of filing bankruptcy is important to understanding when bankruptcy estate planning becomes unlawful. All insolvent individuals approach the day of filing as essentially one of three characterized types. Nimmer, supra note 2, at 101. Debtors can be classified as “natural” debtors, “intuitive” debtors, and “counseled” debtors. Id.

The natural debtor, harassed by creditors, naive and uncounseled, does not attempt to alter his economic condition in contemplation of bankruptcy. Such planning may be impossible due to the debtor's poverty, or the planning may be unnecessary in light of the fact that the debtor owns no property in excess of that allowed by federal or state exemption law. The natural debtor receives no pre-bankruptcy counseling. As a result, the debtor files bankruptcy in a "truly natural condition." The natural debtor is the type most seen in consumer bankruptcy cases. Id.

The intuitive debtor is acutely aware of his deteriorating financial condition and of the possibility of future bankruptcy. This debtor possesses actual or intuitive knowledge as to the priority or nature of his debts and property. Accordingly, the intuitive debtor transfers assets to certain favored creditors in order to optimize his current and possible future positions. The intuitive debtor comes to his attorney "structured for bankruptcy." The only issue that his attorney must resolve is how to minimize potential harm to the debtor by timing the filing of his bankruptcy petition.
accepted rule is that such conversions are not, per se, a fraud upon creditors, even where the motivation is to place property beyond the reach of creditors.92 The per se rule is supported by general legal principles which require that an alleged fraud must be clearly shown and cannot be presumed.93 A creditor challenging a debtor’s bankruptcy estate planning must therefore show something more than the mere fact of conversion in order to prevail.94

Justifications offered by debtors and courts suggest various reasons supporting the per se rule. One approach posits that the per se rule is justified because the legislation conferring exemptions is absolute and without exception.95 This approach is consistent with the general doctrine that exemption laws are to be liberally construed in favor of the debtor.96 Furthermore, debtors are encouraged to make full use of all available exemptions.97

A variation of this approach appears in First Nat’l Bank of Humboldt v. Glass,98 where a pseudo assumption of risk theory is used. In Glass, the court explained that credit was extended to the debtor notwithstanding the debtor’s then existing exemption rights.99 Since credi-

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92. See Ford v. Poston (In re Ford), 773 F.2d 52, 54 (4th Cir. 1985); Armstrong v. Lindberg (In re Lindberg), 735 F.2d 1087, 1090 (8th Cir. 1984), cert. denied, 469 U.S. 1073 (1984); First Texas Sav. Ass’n v. Reed (In re Reed), 700 F.2d 986, 990 (5th Cir. 1983); Bank of Pennsylvania v. Aldman (In re Adlman), 541 F.2d 999, 1004 (2d Cir. 1976); Grover v. Jackson (In re Jackson), 472 F.2d 589, 590 (9th Cir. 1973); Forsberg v. Security State Bank, 15 F.2d 499, 501 (8th Cir. 1926); First Nat’l Bank of Humboldt v. Glass, 79 F. 706, 707 (8th Cir. 1897).


94. Forsberg, 15 F.2d at 502. (“[B]efore the existence of such fraudulent purpose can be properly found, there must appear in evidence some facts or circumstances which are extrinsic to the mere facts of conversion of nonexempt assets into exempt and which are indicative of such fraudulent purpose.”) Accord, In re Adelman, 541 F.2d 999 (2d Cir. 1976); In re Ellingson, 63 Bankr. 271 (Bankr. N.D. Iowa 1986).

95. Crawford v. Sternberg, 220 F. 73, 76–77 (8th Cir. 1915); Resnick, supra note 47, at 630.

96. Reduction, supra note 61, at 148.

97. Id.; In re Lindberg, 735 F.2d at 1090.

98. 79 F. 706 (8th Cir. 1897).

99. Id. at 707.
tors are presumed to know as much about exemption law as debtors, creditors necessarily assume the risk that debtors will obtain exempt property when experiencing financial stress. However, this approach presumes that the purchase of exempt property is a considered risk of extending credit. At least one commentator has argued that this may be a risk that creditors should not be required to bear. In any event, if creditors are to be deemed to have assumed this risk they are entitled to know what that risk entails.

Another approach notes that a debtor's conduct in converting nonexempt property to exempt property affects no interest secured by law for creditors. Rather, the debtor is held to be merely exercising common law rights of dominion over his property. In its simplest terms, fraud cannot be predicated on an act permitted by law. This premise appears in Forsberg v. Security State Bank, where the court held that a debtor's trade of nonexempt cattle for exempt hogs was not a fraud upon creditors. The court noted that while the transaction allowed the debtor to increase his exemptions, the debtor "should [not] be penalized for merely doing what the law allows him to do." The court stated further that in order to find a fraudulent purpose "there must appear in evidence some facts or circumstances which are extrinsic to the mere facts of conversion of nonexempt assets into exempt and which are indicative of such fraudulent purpose."

100. Id.; Resnick, supra note 47, at 631.
102. The Minnesota Supreme Court stated:
A debtor in securing a homestead for himself and family, by purchasing a house with non-exempt assets, or by moving into a house which he already owns, takes nothing from his creditors which the law secure to them, or in which they have any vested right. He merely puts his property into a shape in which it will be the subject of a beneficial provision for himself, which the law recognizes and allows. Even if he disposes of his property subject to execution, for the very purpose of converting the proceeds into exempt property, this will not constitute legal fraud. This he may do at any time before the creditors acquire a lien upon the property. It is a right which the law gives him, subject to which every one gives him credit, and fraud can never be predicated on an act which the law permits.

Jacoby v. Parkland Distilling Co., 41 Minn. 227, 229–30, 43 N.W. 52, 52 (1889). While Jacoby involved only a homestead exemption, its underlying principle has been applied to cases involving non-homestead exemptions. See, e.g., Forsberg v. Security State Bank, 15 F.2d 499, 500–01 (8th Cir. 1926) (applying South Dakota law); Crawford v. Sternberg, 220 F. 73, 76 (8th Cir. 1915) (applying Arkansas law).

103. Jacoby, 41 Minn. at 229–30, 43 N.W. at 52.
104. Id. at 230, 43 N.W. at 52.
105. 15 F.2d 499 (8th Cir. 1926).
106. Id. at 501.
107. Id.
108. Id. at 502. See also Norwest Bank Nebraska v. Tveten, 848 F.2d 871, 874–75 (8th Cir. 1988) (citing with approval the rule from Forsberg).
An oft-cited justification for the judicial countenance of these conversions is the House and Senate reports regarding exemption rights. Based upon hearings on the matter, both House and Senate reports state:

As under current law, the debtor will be permitted to convert nonexempt property into exempt property before filing a bankruptcy petition. The practice is not fraudulent as to creditors, and permits the debtor to make full use of the exemptions to which he is entitled under the law.109

Debtors have, in some cases, argued that this congressional statement is a broad endorsement of the right to convert nonexempt assets to exempt assets on the eve of bankruptcy.110 The proposition is, however, of doubtful validity. Not only does the statement overstate the judicial rule,111 but the Bankruptcy Code does not even expressly deal with the question.112 Interestingly enough, several members of Congress urged that eve of bankruptcy conversions of nonexempt property to exempt property be disallowed in view of the potential for abuse.113 This opposition was based on the belief that creditors expect that a debtor's assets be available for distribution in the event of a bankruptcy. However, the per se rule, as reflected in the House and Senate reports, mitigates the unfairness and non-uniformity that would result from an outright interdiction of the practice of bankruptcy estate planning. This unfairness and non-uniformity would result from the diverse exemption statutes of the individual states. While debtors in liberal exemption states may not be unduly prejudiced by the prohibition of bankruptcy estate planning, debtors in limited exemption states would face the prospect of having minimal exemptions.114 As such, it seems reasonable that Congress intended to allow bankruptcy estate planning in order to protect debtors in those states having minimal exemptions.115


111. Hardin, supra note 42, at 724.

112. See Mickelson v. Anderson (In re Anderson), 31 Bankr. 635, 637 (Bankr. D. Minn. 1982) (Committee Reports are often ambiguous and confusing, often contradictory and sometimes in total error when applied to the end legislative product).


114. Id. at ¶ 522-42.

115. Id. at ¶ 522-42 n.24 (citing Proposed Bankruptcy Act Revision: Hearings on H.R.
B. Denial of Discharge for Bankruptcy Estate Planning

While the per se rule recognizes a debtor's right to manipulate property prior to bankruptcy, not every bankruptcy estate planning transaction is proper. The prospect of having discharge denied has become a caveat to all debtors that, notwithstanding the validity of an exemption obtained on the eve of bankruptcy, a grant of discharge is not always assured.

1. The Intent Clause

The granting of a discharge, unlike the validity of exemptions, is a matter determined solely by federal law pursuant to section 727 of the Bankruptcy Code. As the per se rule instructs that conversion without more is not improper, section 727 answers in part the question left open by the per se rule. What more is needed? The partial answer is intent; specifically, the intent to hinder, delay, or defraud creditors. The unanswered part is what type of conduct constitutes this intent?

The purpose behind section 727(a)(2)(A) is to punish debtors who, with the proscribed intent, transfer property that would otherwise be property of the bankruptcy estate. A party objecting to discharge carries the initial burden of proving four statutory elements: (1) that a transfer of property has occurred, made by the

31 and H.R. 32 Before the Subcommittee on Civil and Constitutional Rights of the Committee on the Judiciary, 94th Cong., 2d Sess. 1282 (1976) (Statement of Hon. Joe Lee)).

116. Hardin, supra note 42, at 728. See, e.g., Norwest Bank Nebraska v. Tveten, 848 F.2d 871, 876 (8th Cir. 1988) (debtor's attempt to shield almost his entire net worth of $700,000 by 17 transfers within three months of filing bankruptcy justifies denial of discharge); Devers v. Bank of Sheridan (In re Devers), 759 F.2d 751, (9th Cir. 1985) (debtor's story that a tractor had just vanished was found incredible by the court, and protection has not allowed); First Texas Sav. Ass'n v. Reed (In re Reed), 700 F.2d 986, 991-92 (5th Cir. 1983) (debtor denied discharge when he rapidly converted nonexempt assets to extinguish one home mortgage and reduce another); Shanks v. Hardin, 101 F.2d 177, 178 (6th Cir. 1939).

117. B. Weintraub & A. Resnick, supra note 1, at 4-36.

118. In re Reed, 700 F.2d, 986, 991 (5th Cir. 1983).

119. Section 727(a)(2)(A) states in part:
   Section 727. Discharge
   (a) The court shall grant discharge, unless— . . .
   (2) the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed, destroyed, mutilated, or concealed, or has permitted to be transferred, removed, destroyed, mutilated, or concealed—
   (A) property of the debtor, within one year before the date of the filing of the petition;

debtor or made at his direction or request; (2) that the transfer involved property of the debtor; (3) that the transfer was made within one year preceding filing a bankruptcy petition; and (4) that the debtor had, contemporaneously with the transfer, the actual intent to hinder, delay, or defraud creditors or the trustee in bankruptcy.\textsuperscript{121} In most conversion cases where an objection to discharge is made, the first three elements are satisfied with relative ease, due in part to the broad definition of the term “transfer.”\textsuperscript{122} Yet, notwithstanding the statute’s conjunctive language which contemplates alternative grounds for denying discharge,\textsuperscript{123} proving the fourth element, the debtor’s actual intent, is a thorny task since it can rarely be established by direct evidence.\textsuperscript{124} Consequently, an objecting party need only adduce facts and circumstances, apart from the conversion into exempt property, from which the debtor’s intent may be inferred.\textsuperscript{125} After this initial burden is met, the burden shifts to the debtor to explain away inferences drawn from the offered proof.\textsuperscript{126} Once the inference of fact of debtor’s actual state of mind is drawn from the circumstantial evidence, the bankruptcy court must determine, as a matter of law, whether the debtor’s state of mind equates with the intent that the statute proscribes.\textsuperscript{127}

\textsuperscript{121} Panuska v. Johnson (\textit{In re} Johnson), 80 Bankr. 953, 957 (Bankr. D. Minn. 1987); Drenckhahn, 77 Bankr. at 704; Clausen, 44 Bankr. at 43.

\textsuperscript{122} The term “transfer” is defined as “every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property, including retention of title as a security interest and foreclosure of the debtor’s equity of redemption.” 11 U.S.C. § 101(50) (1982 & Supp. IV 1986). \textit{See also} S. REP. No. 95-989, 95th Cong., 2d Sess. 26–27 (1978), \textit{reprinted} in 1978 U.S. CODE CONG. & ADMIN. NEWS 5787, 5813; H.R. REP. No. 95-595, 95th Cong., 1st Sess. 313–14 (1977), \textit{reprinted} in 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6271.

\textsuperscript{123} Under § 727(a)(2)(A), discharge may be denied where the debtor has, within one year before the date of filing the petition, transferred property with the intent to hinder, or to delay, or to defraud creditors. \textit{See supra} note 119 for the text of the statute.

\textsuperscript{124} Wilder Health Care Center v. Elholm (\textit{In re} Elholm), 80 Bankr. 964, 968 (Bankr. D. Minn. 1987); Norwest Bank Nebraska v. Tveten (\textit{In re} Tveten), 70 Bankr. 529, 532 (8th Cir. 1988); \textit{see also} Caspers v. Van Horne (\textit{In re} Van Horne), 823 F.2d 1285, 1287 (8th Cir. 1987) (applying same principle in dischargeability proceedings under 11 U.S.C. § 523(a)(2)(A)).

\textsuperscript{125} \textit{See} First Beverly Bank v. Adeebe (\textit{In re} Adeebe), 787 F.2d 1339, 1343 (9th Cir. 1986); Salomon v. Kaiser (\textit{In re} Kaiser), 722 F.2d 1574, 1582 (2d Cir. 1983); First Texas Sav. Ass’n v. Reed (\textit{In re} Reed), 700 F.2d 986, 991–92 (5th Cir. 1983).


\textsuperscript{127} \textit{In re} Elholm, 80 Bankr. at 968.
There is a split of opinion, however, as to the proper standard of proof to be applied in objections to discharge under section 727. A number of bankruptcy courts hold that an objection to discharge, like many other issues in civil litigation, requires the objecting party to only prove the debtor’s intent by a preponderance of the evidence.\(^{128}\) In contrast, many other bankruptcy courts hold that the severity of denying discharge warrants the application of the clear and convincing standard of establishing the proof of conduct justifying a denial of discharge.\(^{129}\)

2. Judicial Treatment of Bankruptcy Estate Planning

In applying the language of section 727, there is little agreement among the bankruptcy courts as to what conduct constitutes the intent to hinder, delay, or defraud where a debtor has converted non-exempt property to exempt property. Naturally, the application of any standard should not be mechanical,\(^{130}\) but the lack of judicial agreement on the matter has prevented the acceptance of a specific meaning of the intent clause of section 727. Without the guidance of any clear standard, bankruptcy courts view the issue of discerning the debtor’s intent from differing angles. Some courts have focused on the debtor’s motivation in acquiring the exempt property.\(^{131}\) The

\(^{128}\) See Farmers Co-op. Ass’n v. Strunk, 671 F.2d 391, 395 (10th Cir. 1982) (an objector must prove by a preponderance of evidence debtor’s intent to hinder, delay, or defraud creditors); Gabrielli v. Shultz (In re Shultz), 28 Bankr. 395, 396 (Bankr. App. 9th Cir. 1983) ("[t]he burden of proof on this issue is the same preponderance of evidence standard that governs ordinary civil litigation"); In re Clausen, 44 Bankr. at 45 ("creditor need only prove its case by a preponderance of the evidence").


\(^{130}\) See Richardson v. Germania Bank, 263 F. 320 (2d Cir. 1919), cert. denied, 252 U.S. 582–83 (1920), wherein the court stated, "[t]he elements productive of that intent, ... can never be defined. They vary as do facts, and any judge or jury, dealing with facts with some rule of thumb, will always miss the human touch. Testimony can never be tested or weighed by machine." Id. at 325.

\(^{131}\) See e.g., Shanks v. Hardin, 101 F.2d 177 (6th Cir. 1939); Kangas v. Robie, 264 F. 92, 94 (8th Cir. 1920); Rameker v. Schwingle (In re Schwingle), 15 Bankr. 291, 294–95 (Bankr. W.D. Wis. 1981); In re Martin, 217 F. Supp. 937, 938 (D. Ore. 1963).
case of *In re Ford* \(^{132}\) illustrates this approach. In *Ford*, the bankruptcy court denied discharge, noting that "the primary motivation for the [debtor's] conversion [from nonexempt to exempt property] was his intention to remove the [property] from the creditor's reach..." \(^{133}\) By negative implication, had the conversion been made with a different motivation, such as the desire to actually own the exempt property, discharge would have been granted. The motivation approach is, at best, a semantic quagmire which has been criticized as inconclusive since many debtor's may have mixed motives. \(^{134}\)

Other bankruptcy courts have relied on the policies behind exemptions to help determine whether the debtor's actions violate section 727. In the case of *In re Zouhar*, \(^{135}\) the debtor sought to shelter nearly $130,000 by converting nonexempt assets into exempt annuities before filing bankruptcy. \(^{136}\) Distinguishing previous cases permitting such conduct as having involved smaller amounts, the bankruptcy court stated, "While a bankrupt is entitled to adjust his affairs so that some planning of one's exemptions under bankruptcy is permitted, a wholesale sheltering of assets which otherwise would go to creditors is not permissible." \(^{137}\) This decision seems justified on the ground that the claimed exemptions were inconsistent with the traditional exemption policy. \(^{138}\) According to the claimed exemptions approach, the denial of discharge is based not on the debtor's conduct or inferred intent, but rather on the amount of claimed exemptions. This approach diverts the bankruptcy court's attention, for it implicitly requires that the bankruptcy court determine, on a case by case basis, the debtor's proper exemption level. At least one federal circuit court has expressly renounced this approach. \(^{139}\)

The approach used by many bankruptcy courts in inferring the debtor's state of mind under section 727 has been the "badges of fraud" analysis. \(^{140}\) This analysis compares the debtor's conduct with the analytical backdrop of the badges of fraud to infer the debtor's

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133. *Id.* at 450.
136. *Id.* at 156.
137. *Id.* at 157.
138. *See supra* notes 61–70 and accompanying text.
139. *See* Smiley v. First Nat'l Bank of Belleville (*In re Smiley*), 864 F.2d 562, 567 (7th Cir. 1989) ("we should not prohibit a debtor's full use of exemptions within the limits of the law").
140. This analysis recognizes that cases decided under the comparable language of section 548 utilize the badges of fraud to ascertain intent in fraudulent transfer cases. Under section 548, the bankruptcy trustee may avoid transfers that were made
intent in engaging in specified conduct. There are six badges of fraud used to infer intent which are as follows: (1) the lack or inadequacy of consideration; (2) the family, friendship, or close associate relationship between the parties; (3) the retention of possession, benefit, or use of the property in question; (4) the financial condition of the party sought to be charged both before and after the transaction in question; (5) the existence or cumulative effect of the pattern or series of transactions or course of conduct after incurring of debt, onset of financial difficulties, or pendency or threat of suits by creditors; and (6) the general chronology of the events and transactions under inquiry. The debtor's actual intent is inferred by the bankruptcy court after specific weight is ascribed to conduct resembling a given badge of fraud in light of all the evidence.

The popularity of the badges of fraud analysis is perhaps explained by its versatility. The broad, expansive language of the badges of fraud make the analysis applicable to almost any constellation of facts imaginable. This is particularly true where the debtor has, with the intent to hinder, delay, or defraud, engaged in a covert pattern of removing assets from the reach of creditors. Such a pattern was found in Fox v. Schmit.

In Fox, not only did the debtor borrow money from a creditor, never intending to repay the loan, but he promised to give the creditor the proceeds from the sale of the debtor's home if the creditor would loan him money to purchase a new home. After selling his home, the debtor kept the proceeds. Later, he liquidated various nonexempt assets to reduce his homestead mortgage after the creditor obtained a judgment against him in state court. Relying on the badges of fraud analysis, the bankruptcy court found that the debtor intended to defraud the judgment creditor. Furthermore, the bankruptcy court added that the debtor's pattern of conduct was designed to frustrate creditor collection efforts and was extrinsic evidence of his intent to hinder and delay creditors.

within one year before the date of filing with the actual intent to hinder, delay, or defraud. 11 U.S.C. § 548(a)(1) (1982 & Supp. IV 1986).

141. See In re Clausen, 44 Bankr. at 44; see also In re May, 12 Bankr. 618, 627 (Bankr. N.D. Fla. 1980). “The 'badges of fraud' that today serve as circumstantial evidence of a debtor's actual intent to hinder, delay or defraud its creditors are the same as those enumerated by the Star Chamber [in England] four centuries ago.” See Cook, Fraudulent Transfer Liability Under the Bankruptcy Code, 17 Hous. L. Rev. 263, 270-71 (1980) (citing Twyne's Case, 76 Eng. Rep. 809 (1601)).

142. See, e.g., In re Tveten, 70 Bankr. 529, 534 (Bankr. D. Minn. 1987).


144. Id. at 590.

145. Id.

146. Id.

147. Id. at 590-91.

148. Id.
A similar pattern of conduct was held to evince an intent to defraud in *First Texas Sav. Ass'n v. Reed*.149 Shortly after arranging with his creditors to be free from the payment of obligations until the following year, the debtor quickly converted nonexempt assets to extinguish one home mortgage and reduce another prior to bankruptcy.150 The debtor also diverted receipts from his business into a bank account not disclosed to his creditors.151 In denying discharge, the appeals court deftly expressed its feelings regarding the debtor’s conduct stating:

It would constitute a perversion of the purposes of the Bankruptcy Code to permit a debtor earning $180,000.00 a year to convert every one of his major nonexempt assets into sheltered property on the eve of bankruptcy with actual intent to defraud his creditors and then emerge washed clean of future obligation by carefully concocted immersion in bankruptcy waters.152

An example of an obvious intent to hinder and delay creditors was found in *McCormick v. Security State Bank*.153 After liquidating nonexempt assets and depositing the proceeds into his wife’s bank account and an out-of-state bank account, the debtor told his banker that he was unable to make any payment on an unsecured note.154 The funds were later used by the debtor to purchase a homestead.155 The debtor’s admitted lie to the bank officer and his concealing of assets were cited as evidence of his intent to hinder and delay creditors.156

If, however, the badges of fraud analysis is to be the judicial litmus test for ascertaining the proscribed intent it is not a marvel of precision. The case of *Hanson v. First Nat’l Bank in Brookings*157 is an illustration of this point. Although *Hanson* involves an objection to a claimed exemption rather than an objection to discharge, the court applies the per se rule and the badges of fraud analysis in the same manner as in an objection to discharge case.

Kenneth and Lucille Hanson filed a joint Chapter 7 petition in United States Bankruptcy Court, District of South Dakota, on November 30, 1983.158 The Hansons were farmers whose financial difficulties led them to default on their loans from First National Bank
in Brookings (the "Bank"). On advice of counsel, the Hansons had much of their nonexempt property appraised and then sold it for the appraised value. In a series of five transactions, the Hansons sold a car, two vans, a motor home, and certain home furnishings to their son and to Kenneth Hanson's brother for a total amount of $34,415. A couple of weeks before filing their bankruptcy petition, the Hansons used most of these proceeds to purchase life insurance policies with cash surrender values of $19,955 and to prepay $11,033 on their homestead mortgage. Under South Dakota law, the homestead exemption is unlimited. The South Dakota exemption for life insurance policies is limited to $20,000.

The Bank asserted that by transferring their property to family members while retaining the use and enjoyment of the property the Hansons committed a "classic badge of fraud." The Hansons explained that the vehicles were still stored on their property because their son, the purchaser, still lived at home. The Hansons admitted that they occasionally used the vehicles, but only with the express permission of their son. The Hansons also admitted that the household goods were stored in their home and explained that this was because Mr. Hanson's brother could not retrieve the goods immediately after the sale.

The bankruptcy court denied the Bank's objection to the claimed exemptions on the grounds that the Hansons' actions were permissible under the law and did not constitute extrinsic evidence of fraud. The district court affirmed the bankruptcy court's order, concluding that it was not clearly erroneous. The Eighth Circuit Court of Appeals also affirmed. The court of appeals determined that even though the Hansons retained use and possession of the property after the sale, there was no evidence of fraudulent intent.

The court reasoned that a debtor is entitled to exempt certain property from claims of his creditors under 11 U.S.C. section 522. The court stated, "When the debtor claims a state created exemp-

159. Id.
160. Id.
161. Id.
162. Id.
165. Id. at 867.
166. Id. at 868.
167. Id.
168. Id.
169. Id.
170. Id.
171. See id. at 868–69.
172. Id. at 868.
tion, the scope of the claim is determined by state law." The court also reasoned that the debtor's conversion of nonexempt property into exempt property "for the express purpose of placing that property beyond the reach of creditors" without extrinsic evidence of fraudulent intent, would not deprive the debtor of the exemption. The court concluded that the bankruptcy court was not clearly erroneous in finding that the debtors did not possess the requisite intent and that the debtors were entitled to claim their homesteaded and insurance contracts as exempt.

There is a common thread running through these cases in that four of the six badges of fraud are invariably present where the debtor engages in bankruptcy estate planning. This tilts the balance unfairly toward finding the proscribed intent warranting denial of discharge in every bankruptcy estate planning case.

III. A COMPARISON OF Tveten and Johnson

A comparison of the factual and legal circumstances of Tveten and Johnson reveals the troubling state currently faced by attorneys and debtors. Although Tveten and Johnson arose in the same jurisdiction and involved similar facts, the results reached were completely opposite.

173. Id.
174. Id.
175. Id. at 869.
176. See Brief for Appellant at 10–15, Norwest Bank Nebraska v. Tveten, 848 F.2d 871 (8th Cir. 1988) (No. 87-5312MN). Where bankruptcy estate planning has resulted in conversions of nonexempt property into exempt property, at least four of the six badges of fraud will exist. Judicial interpretation and the broad nature of the badges of fraud makes this inevitable.

Badge 3, retaining the possession, benefit, or use of the property, will exist since this is a result of exemptions. Badge 4, financial condition before and after the transaction, examines whether the debtor was rendered insolvent because of the transaction. In a bankruptcy estate planning case, the debtor's net worth would remain the same notwithstanding the depletion of the pool of assets available for distribution. Badge 5, the effect of a course or pattern of conduct after the onset of financial difficulties, will always be present when a debtor moves to convert more than one item of nonexempt property to exempt property. To rule otherwise differentiates between debtors converting to exempt property within bankruptcy and those debtors doing the same outside of bankruptcy. Badge 6, the general chronology of the transactions, looks at the timing of the conversion to exempt property. When the conversion is on the eve of bankruptcy, this badge will also always be present.

Badges 1 and 2 may also appear in bankruptcy estate planning cases, but those badges examine transfers where the property is secretly being held by a third person. Id.
A. Norwest Bank Nebraska v. Tveten

1. The Bankruptcy Court Decision

Omar Tveten was a physician who became involved as an investor-principal in a corporation engaged in various commercial investment activities. Tveten personally guaranteed most of the corporation's major indebtedness. Tveten's financial troubles began in 1985 when several of his business investments failed, resulting in substantial personal liability on promissory notes and guarantees. After several lawsuits were brought to enforce these obligations, Tveten consulted with an attorney. Three months before filing his bankruptcy petition, as part of his bankruptcy estate planning, Tveten liquidated nonexempt assets and invested the proceeds in annuities and life insurance contracts which were exempt under Minnesota law. After converting approximately $700,000 of nonexempt property into exempt property, Tveten filed a petition under Chapter 11 of the Bankruptcy Code seeking to discharge nearly $19,000,000 in debts and guaranty obligations.

After being notified of Tveten's bankruptcy, several creditors objected to discharge pursuant to 11 U.S.C. section 727(a)(2)(A). Emphasizing that Tveten was an unmarried physician with substantial benefits payable from a fraternal benefit society that were exempt from creditor claims under Minnesota law. At the time, benefits payable from a fraternal benefit society were, without a dollar limitation, exempt from creditor claims under Minnesota law. See Minn. Stat. §§ 550.37, 64B.18 (1986).

The objections to Tveten's claimed exemptions prompted the bankruptcy court to certify four questions of law to the Minnesota Supreme Court regarding the validity of those exemptions under Minnesota law. The objections to Tveten's claimed exemptions prompted the bankruptcy court to certify four questions of law to the Minnesota Supreme Court regarding the validity of those exemptions under Minnesota law. See In re Tveten, 70 Bankr. at 530-31. In its findings of fact, the bankruptcy court found that Tveten made seventeen transfers of nonexempt assets to exempt assets between September 28, 1985 and January 7, 1986. These included transfers of land and cattle to relatives, the sale of property to a business partner, and the sale of securities. In his bankruptcy petition filed on January 7, 1986, Tveten claimed as exempt, annuities and life insurance contracts valued at $531,538.54.

177. Norwest Bank Nebraska v. Tveten, 848 F.2d 871, 872 (8th Cir. 1988).
178. Id.
179. See Brief for Appellant at 3-7, Norwest Bank Nebraska v. Tveten, 848 F.2d 871 (8th Cir. 1988) (No. 87-5312MN).
180. Id. at 873. At the time, benefits payable from a fraternal benefit society were, without a dollar limitation, exempt from creditor claims under Minnesota law. See Minn. Stat. §§ 550.37, 64B.18 (1986).
181. The exact amount of debt and guaranty obligations was $18,920,000. In re Tveten, 70 Bankr. at 530-31. In its findings of fact, the bankruptcy court found that Tveten made seventeen transfers of nonexempt assets to exempt assets between September 28, 1985 and January 7, 1986. Id. These included transfers of land and cattle to relatives, the sale of property to a business partner, and the sale of securities. Id. In his bankruptcy petition filed on January 7, 1986, Tveten claimed as exempt, annuities and life insurance contracts valued at $531,538.54. Id.
182. In re Tveten, 70 Bankr. at 532. In a Chapter 11 case, confirmation of a plan ordinarily constitutes discharge under 11 U.S.C. § 1141(d)(1). Under 11 U.S.C. § 1141(d)(3)(C), however, the confirmation of a plan does not discharge a debtor if the debtor would be denied a discharge under § 727(a) had the case been filed under Chapter 7.
tial income and no dependents, the creditors argued that the "sheer magnitude and timing of the conversions in light of Tveten's pursuit by creditors, supplies the necessary extrinsic evidence that the debtor's intent was to hinder, delay, or defraud his creditors." Tveten admitted that the transfers were made to place the property outside the reach of his creditors. Tveten argued, however, that the specific acts of extrinsic fraud found in previous cases were not present in his case. Pursuant to section 1141(d)(3), the bankruptcy court concluded that Tveten would have been denied discharge under section 727(a) of the Bankruptcy Code if his case had arisen under Chapter 7.

Citing First Texas Sav. Ass'n v. Reed, and relying on the badges of fraud analysis, the bankruptcy court concluded that the transfers of land to relatives and associates, coupled with the rapid liquidation of nonexempt assets while facing extensive personal liability, amounted to "nothing more than an attempt to defraud creditors and an abuse of the Bankruptcy Code." Distinguishing Forsberg v. Security State Bank as a case where "the debtor converted property . . . to take advantage of the reasonable exemptions," the bankruptcy court stressed that Tveten converted substantial amounts of property into assets which he now claimed as exempt. Relying on Tveten's own admission that property was transferred to place it out of creditor's reach, the bankruptcy court found this to be, as in First Beverly Bank v. Adeeb, an admission of the intent to hinder and delay creditors.

184. Tveten, 70 Bankr. at 530.
186. Tveten, 70 Bankr. at 535.
187. 700 F.2d 986 (5th Cir. 1983).
188. Tveten, 70 Bankr. at 534.
189. Id. (emphasis added).
190. Id.
191. (In re Adeeb), 787 F.2d 1339, 1343 (9th Cir. 1986). In Adeeb, the debtor acted on advice of counsel in transferring real estate to some "trusted" friends. Id. at 1341. After speaking with a second attorney, the debtor started reversing the transfers but was forced into bankruptcy before he completed the reversal. Id. In finding an intent to hinder or delay creditors, the appeals court stated, "When a debtor admits that he acted with the intent penalized by section 727(a)(2)(A), there is no need for the court to rely on circumstantial evidence or inferences in determining whether the debtor had the requisite intent." In re Adeeb, 787 F.2d at 1343, quoted in In re Tveten, 70 Bankr. at 534-35.
2. The Eighth Circuit Court of Appeals Decision

After an unsuccessful appeal to the district court,192 Tveten sought review of the case by the Eighth Circuit Court of Appeals to determine whether there was extrinsic evidence demonstrating the intent to defraud creditors.193 After distinguishing between the debtor's right to claim exempt property and the debtor's right to discharge, the court of appeals reviewed prior cases involving bankruptcy estate planning.194 The court of appeals noted that, in those cases where discharge was granted, by limiting the monetary value of the exemptions, the claimed exemptions comported with the federal fresh start policy.195 This policy, according to the court of appeals, "has been explicit, or at least implicit, in these cases."196 Citing Forberg v. Security State Bank197 and In re Ellingston198 as precedent, the court of appeals reasoned that exemptions with a limited monetary value accord with the federal fresh start policy.199 By comparison, the court implied that an unlimited state exemption does not comport with either social or fresh start policies.200 The court of appeals stated that, by converting over $700,000 worth of nonexempt property into exempt property, "Tveten did not want a mere fresh start, he wanted a head start."201

Holding that the bankruptcy court's finding of fraudulent intent was not clearly erroneous,202 the court of appeals agreed with the bankruptcy court's findings that Tveten's entire pattern of conduct demonstrated fraudulent intent rather than astute bankruptcy estate planning.203 In closing, the court of appeals distinguished the result in Tveten from that reached the same day in Hanson v. First Nat'l Bank in Brookings,204 describing Hanson as a case falling "within the myriad of cases which have permitted such a conversion on the eve of bank-

192. The bankruptcy court decision in In re Tveten, 70 Bankr. 529 (Bankr. D. Minn 1987) was affirmed by the district court. In re Tveten, 82 Bankr. 95 (D. Minn. 1987).
194. Id. at 874–75.
195. Id. at 875.
196. Id.
197. 15 F.2d 499, 501 (8th Cir. 1926) ("the policy of [exemption] statutes is to favor the debtors, at the expense of creditors, in the limited amounts allowed them").
198. 63 Bankr. 271, 277–78 (Bankr. N.D. Iowa 1986) (the bankruptcy court found that the debtor's acquisition and improvement of exempt property consistent with the social policies underlying exemptions); Resnick, supra note 47, at 621.
199. Tveten, 848 F.2d at 876.
200. "In the instant case, however, the state exemption relied on by Tveten was unlimited, with the potential for unlimited abuse." Id. at 876.
201. Id. (quoting In re Zouhar, 10 Bankr. 154, 156 (Bankr. D.N.M. 1981).
202. Id. at 876–77.
203. Id.
204. 848 F.2d 866 (8th Cir. 1988).
ruptcy." 205 This superficial treatment of Hanson provides the catalyst for Judge Arnold’s thoughtful dissent. 206

3. The Dissenting Opinion

The dissent in Tveten addressed two primary failings of the majority opinion. First, the dissent argued that there is no evidence of any devious conduct by Tveten evincing a fraudulent intent. 207 The dissent pointed out that unlike the debtors in First Texas Sav. Ass’n v. Reed or McCormick v. Security State Bank, Tveten neither lied to nor mislead his creditors, nor transferred property for less than fair value. 208 The dissent also noted that the majority opinion did not cite to any such conduct by Tveten. 209

Secondly, the dissent revealed the underlying “separation of powers” issue raised by the majority opinion. 210 “[W]hether exemptions are limited in amount is a legislative question ordinarily to be decided by the people’s elected representatives. . . . [T]he problem is simply not one susceptible of a judicial solution according to manageable objective standards.” 211 Expressing its depreciation, the dissent likened the majority’s reasoning to the statement that “there is a principle of too much; phrased colloquially, when a pig becomes a hog it is slaughtered.” 212 This reasoning, argued the dissent, leaves the distinction between permissible and impermissible claims of exemption to each bankruptcy judge’s own sense of proportion. 213

4. An Analysis of the Reasoning in Tveten

Although the equities in Tveten favor the result reached and affirmed by the court of appeals, the legal analysis is questionable. Additionally, the court of appeals erroneously concluded that Tveten’s

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205. Tveten, 848 F.2d at 876.
206. Id. at 878–79. See also, Hanson, 848 F.2d at 870 (Arnold, J., concurring). In his concurring opinion in Hanson, Judge Arnold remarks that the court’s attempt to reconcile Hanson with Tveten is flawed:

The result, in practice, appears to be this: a debtor will be allowed to convert property into exempt form, or not, depending on findings of fact made in the court of first instance, the Bankruptcy Court, and these findings will turn on whether the Bankruptcy Court regards the amount of money involved as too much. With all deference, that is not a rule of law. It is simply a license to make distinctions among debtors based on subjective considerations that will vary more widely than the length of the chancellor’s foot.

Id. at 870–71.
207. Tveten, 848 F.2d at 878 (Arnold, J., dissenting).
208. Id.
209. Id. at 878.
210. Id.
211. Id. at 878–79.
212. Id. at 879 (citing In re Zouhar, 10 Bankr. 154, 157 (Bankr. D.N.M. 1981)).
213. Id.
creditors would have little to divide if discharge were granted after
the conversion of assets. Moreover, both the bankruptcy court
and the court of appeals avoided careful examination of the underly-
ing issue. Though it is generally agreed that the conversion of non-
exempt property into exempt property to place it out of creditors’
reach is not, without more, unlawful, there is little agreement
among the courts as to what more is needed to prove the existence of
the proscribed intent. The disparate judicial treatment of this issue
has reduced the bankruptcy court’s inquiry to an ad hoc “I know it
when I see it” standard for finding the proscribed intent. This dispa-
rate treatment is evident in the Tveten decisions which, in effect, offer
differing reasons sustaining the same result.

Faced with a debtor who did not fit the traditional “honest but
unfortunate” mold, who took full advantage of generous state ex-
emption statutes, and who possessed significant future earning po-
tential, both the bankruptcy court and court of appeals implied fraud
in law where it did not exist in fact. Obviously troubled by the
amount of exempt property acquired, the court of appeals supports
its decision by properly noting that the “exemption relied on by
Tveten was unlimited, with the potential for unlimited abuse.” Although this is undeniable, it was not by Tveten’s hand that this
unlimited exemption became law. Moreover, the dollar amount of
the exemption was not the issue presented for review. By addressing
the dollar amount of the exemption, the court of appeals defines the
debtor’s fresh start in terms of the amount of allowable exemptions.
Under such a definition, the freshest fresh start that any debtor could
hope to obtain would be by claiming exemptions to the fullest extent
under existing law. This is exactly what Tveten did. To deny dis-
charge is to say that Tveten and his attorney should have known that
the Minnesota Legislature was wrong to have passed an unlimited
exemption. While the potential for abuse may be present, punishing
instances of debtor overreaching does not solve the problem
presented by the unlimited exemption.

Furthermore, while the court of appeals suggests that Tveten’s
claimed exemption did not further any cognizable social policy,
there is no discussion or analysis of how or why Tveten’s conduct
went “well beyond the purpose for which exemptions are permit-

214. Id. at 876. In his original bankruptcy petitions and schedules, Omar Tveten
listed debts of $17,528,893.00 and property of $1,913,241.99 of which $776,058.54
was claimed as exempt. This would leave $1,137,183.49 for distribution to creditors.

215. See cases cited supra note 92.

216. Tveten, 848 F.2d at 876.

217. The court stated, “His attempt to shield property worth approximately
$700,000 goes well beyond the purpose for which exemptions are permitted.” Id.
The lack of discussion on this point presupposes that informed debtors know the limits to which exemptions can be stretched. Less informed debtors, still believing that they are following the law, will continue to be mislead by unlimited exemptions.

In contrast to the appellate holding, the bankruptcy court not only found fraudulent intent, but equated the debtor's admitted purpose in acquiring exempt property with the pernicious intent to hinder and delay creditors. Despite settled case law holding that a fraud cannot be predicated upon an act permitted by law, the bankruptcy court inexplicably concluded that a finding of intent to hinder and delay may be predicated upon an act permitted by law. This conclusion was also not discussed by the court of appeals.

To find the intent to hinder and delay creditors, the bankruptcy court specifically relied on Tveten's admission that the purchases of exempt property were intended to place property outside the reach of creditors. However, this reliance is misplaced and ignores the resulting and beneficial effects of any purchase of exempt property. These are different sides of the same coin.

The resulting effect of purchasing exempt property is that the debtor keeps the property notwithstanding financial uncertainties. This resulting effect preserves the debtor's ownership of the property. In contrast, the beneficial effect of purchasing exempt property is that the property cannot be used to satisfy a creditor's claim: it is removed from the creditor's reach. Notice, however, that both of these effects occur regardless of the debtor's intent in acquiring the exempt property. A debtor stating that a purchase of exempt property was intended to place property beyond a creditor's reach admits to nothing but the obvious result and corresponding benefit attributed by law to any such acquisition.

By relying on Tveten's statement, the bankruptcy court's reasoning suggests that the transfer was improper since only the beneficial effects of exemption were sought. In other words, it was wrong for Tveten to desire the obvious and implicit benefit of purchasing exempt property. This reasoning is reminiscent of the motivation approach applied to determine whether an asset conversion was

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218. Id.
220. In re Tveten, 70 Bankr. at 535. “Like the debtor in Adeeb, Tveten admits to transferring the property to place it out of the reach of creditors. I find that Tveten acted with the requisite intent to hinder and delay his creditors.” Id.
221. As the court in Reed points out: “While pre-bankruptcy conversion of nonexempt into exempt assets is frequently motivated by the intent to put those assets beyond the reach of creditors, which is, after all, the function of an exemption, evidence of actual intent to defraud creditors is required to support a finding sufficient to deny discharge.” First Texas Sav. Ass'n v. Reed (In re Reed), 700 F.2d 986, 991 (5th Cir. 1983) (emphasis added).
intended to defraud creditors. Whatever Tveten’s motivations, it is disingenuous to predicate the finding of actual intent to hinder and delay upon the debtor’s statement of an obvious function of an exemption. A rule which denies discharge where a debtor’s motive is to shield assets rewards debtors for ignorance of the law and penalizes knowledgeable debtors taking advantage of their full rights under the law.

The soundness of the bankruptcy court and court of appeals decisions is not enhanced by the fact that the exemption statute was found unconstitutional by the Minnesota Supreme Court. While agreeing that, under Minnesota law, a debtor may convert nonexempt property into exempt property before bankruptcy, the Minnesota Supreme Court held that the exemptions claimed by Tveten violated the Minnesota Constitution. The exemption was unconstitutional in that it was not limited to a “reasonable amount” of property, and, insofar as it gave absolute exemption regardless of value to annuity contracts and life insurance purchased from fraternal benefit association. This does not change matters in the bankruptcy context for it is possible to deny discharge just as readily with a limited exemption as an unlimited one. Tveten’s conduct would have been perceived the same.

Its ballyhoo and saber rattling aside, Tveten was merely a Pyrrhic victory for the objecting creditors in the case. While Tveten was ultimately granted discharge under Chapter 11, whether Tveten received the sacrosanct fresh start is an open question.

222. As one commentator remarks about the motivational approach, “[a]n asset conversion case should not turn on the skillful questioning of an attorney or the artful answer of the debtor.” Hardin, supra note 42, at 737.


224. In re Tveten, 402 N.W.2d 551, 558 (Minn. 1987).

225. Id. at 560.


The confirmation of a plan does not discharge a debtor if—
(A) the plan provides for a liquidation of all or substantially all of the property of the estate;
(B) the debtor does not engage in business after consummation of the plan; and
(C) the debtor would be denied a discharge under § 727(a) if the case were a case under Chapter 7.


If all three conditions exist, the confirmation of a plan will not operate as a discharge. Although in its original decision the bankruptcy court concluded that Tveten would have been denied a discharge if the case had been a chapter 7 case, Tveten was ultimately granted discharge because the other two conditions of section 1143(d)(3) did not exist. See id.

228. Omar A. Tveten, at the time of discharge, was a 60-year-old medical doctor.
B. Panuska v. Johnson (In re Johnson)

1. The Bankruptcy Court Decision

Robert Johnson, like Omar Tveten, was a physician who became involved as an investor-principal in a corporation engaged in various commercial investment activities. Johnson, like Tveten, personally guaranteed most of the corporation’s major indebtedness. After judgments were entered against him, Johnson, acting upon the advice of counsel, sold nonexempt property and purchased exempt property with the proceeds. After filing for bankruptcy under Chapter 7, Johnson’s creditors objected to discharge on the ground that the conversion of nonexempt property to exempt property was done with the intent to hinder, delay, or defraud creditors. Like Tveten, Johnson admitted that his conduct was intended to place who had been engaged as the sole practitioner of a medical clinic since 1958. Tveten has liquidated all of his nonexempt property of value, except his clinic. As a consequence of his bankruptcy estate planning, Tveten no longer owns any investment or income producing real estate or ventures except for his medical practice. His practice serves primarily individuals on public assistance and persons without medical insurance. Tveten is not a medical specialist and, due to high malpractice insurance costs, he may be forced to restrict his practice further.

Tveten’s practice has also recently been subject to investigation by the Minnesota Board of Medical Examiners. Fines and restrictions have been imposed upon by the Board of Medical Examiners. As a result, “it is anticipated that Dr. Tveten’s income from the practice of medicine will not increase, and may decline, over the next five years.” See In re Omar A. Tveten, Bky. No. 4-86-30 (Bankr. D. Minn. Feb. 2, 1989) (debtor’s disclosure statement).


230. Id.

231. Id. at 955-56. The bankruptcy court found Johnson made seven transfers of nonexempt property to exempt property between June, 1985, and January 8, 1986. Id. These transfers included: the liquidation of stocks and bank accounts to pay off the first mortgage on his homestead; using proceeds from his interest in his medical partnership to pay off a second mortgage and a marriage dissolution lien against his homestead; selling interests in certain limited partnerships to purchase annuities of $231,905.32, a whole life insurance policy of $4,000.00, and an IRA of $3,978.90; trading antique furniture and other property for one baby grand piano; trading a collection of wooden boats valued around $8,000 for a harpsicord of European manufacture; selling household furnishings, an automobile, a vintage wooden boat, and his boat slip to his live-in girlfriend and depositing the proceeds into his annuity account and/or IRA. Id.

232. Id. at 957. After electing the exemptions available under Minnesota law, Johnson claimed as exempt his full equity interest in his homestead, his IRA account and annuities, his pension and profit-sharing plans, and his musical instruments. Id. at 956. The homestead was valued at $285,000. Id. at 955 n.3. The Chapter 7 Trustee and the creditors filed objections to the claimed exemptions. These objections were continued pending the certification to the Minnesota Supreme Court of the issues ultimately decided in In re Tveten, 402 N.W.2d 551 (Minn. 1988), regarding the constitutionality of the exemptions. Id. at 956; see supra note 7.
property beyond the reach of his creditors.\(^\text{233}\)

Noting that Johnson’s state of mind did “not embody the deceptive animus that is the avatar of an intent to defraud,” the bankruptcy court concluded that the facts did not support a conclusion of actual intent to defraud.\(^\text{234}\) The bankruptcy court then undertook a lengthy discussion to determine whether Johnson’s express intent to put his wealth beyond the reach of creditors constituted an intent to hinder or delay creditors.\(^\text{235}\) The bankruptcy court remarked that from a layman’s perspective, one could say that Johnson’s specific intent was one to hinder, or at least delay, his creditors from seizing property to apply to his debts.\(^\text{236}\) However, conduct constituting the intent to hinder or delay in the bankruptcy context must be determined in light of the punitive function of the statute denying discharge.\(^\text{237}\) As such, the bankruptcy court determined that denials of discharge for pre-petition conduct should be limited to those cases where the debtor’s actions are truly blameworthy in an equitable sense.\(^\text{238}\) Finding that Johnson did nothing more than exercise a prerogative that was fully his under the law, the bankruptcy court held that Johnson’s “bankruptcy estate planning” did not evince the intent that merits the harshest sanction in bankruptcy.\(^\text{239}\) To rule otherwise would frustrate statutory exemption rights by chilling their full exercise.\(^\text{240}\)

After an affirmation at the district court level,\(^\text{241}\) the case was subsequently appealed to the Eighth Circuit Court of Appeals where the objecting creditors argued that the holding in \textit{Tveten} mandated a reversal.\(^\text{242}\) In support of this argument, the creditors argued that \textit{Tveten} distinguished between policy-justified conversions and abusive conversions,\(^\text{243}\) and that there was no meaningful difference between the conduct at issue in \textit{Johnson} or in \textit{Tveten}.\(^\text{244}\) Interestingly, Johnson also points to \textit{Tveten} as controlling, but Johnson insists that \textit{Tveten} mandates an affirmation by the appellate court.\(^\text{245}\)

\begin{itemize}
  \item \textbf{233.} \textit{Johnson}, 80 Bankr. at 956.
  \item \textbf{234.} \textit{Id.} at 959.
  \item \textbf{235.} \textit{Id.}
  \item \textbf{236.} \textit{Id.}
  \item \textbf{237.} \textit{Id.} at 960.
  \item \textbf{238.} \textit{Id.}
  \item \textbf{239.} \textit{Id.} at 960-61.
  \item \textbf{240.} \textit{Id.} at 963.
  \item \textbf{242.} Brief for Appellant at 10, Panuska v. Johnson, (8th Cir. 1989) (No. 88-5296MN).
  \item \textbf{243.} \textit{Id.} at 16.
  \item \textbf{244.} \textit{Id.} at 9.
  \item \textbf{245.} Brief for Appellee at 12, Panuska v. Johnson, (8th Cir. 1989) (No. 88-5296MN).
\end{itemize}
2. An Analysis of the Reasoning in Johnson

Much of the Johnson opinion is a colloquy discussing which test should be applied to cases involving bankruptcy estate planning where the transfers can range from a few dollars to large amounts of money. Rejecting the badges of fraud test as lacking utility, the bankruptcy court attempted to articulate a workable standard for application in bankruptcy estate planning cases. However, the standard articulated and applied by the bankruptcy court in Johnson may have overstepped the very language it seeks to interpret.

Troubled by the tension between bankruptcy estate planning and proscriptions against such planning with the objectionable intent, the bankruptcy court outlined three options for dealing with bankruptcy estate planning cases: denying discharge in all such cases; formulating a standard to deny discharge in some cases but not others; or granting discharge unless an act of actual fraud or the presence of a malign, directed intent to hinder or delay creditors is found. Johnson adopted the last approach.

While the conduct at issue was designed to put the debtor's wealth beyond the reach of creditors, the bankruptcy court concluded that the "[d]ebtor's actual state of mind does not embody the deceptive animus that is the avatar of an intent to defraud." Actual fraud, stated the court, "involves moral turpitude . . . it connotes deceit, artifice, or trick which involves a direct and active operation of intellect which is designed to mislead." Under this standard, the debtor is free to plan his exemptions in contemplation of bankruptcy at the expense of creditor's expectations. All that is required is that the exemption be lawful and the debtor not commit actual fraud or possess a malign, directed intent to hinder or delay his creditors. Deference is thus accorded to legislative determinations and judicial interference is curtailed. This standard, however, does not necessarily follow from the statute. The language of section 727(a) does not require a showing of actual fraud or malign, directed intent to hinder or delay. Rather, a showing of an actual intent to defraud or to hinder or delay is all that the statute requires.

Recognizing this flaw, other bankruptcy courts have rejected the standard enunciated and applied in Johnson. In the case of In re Oberst the holding in Johnson is criticized as negating the express,

246. Johnson, 80 Bankr. at 961-63.
247. Id. at 963 n.14.
248. Id. at 959-63.
249. Id. at 962.
250. Id. at 959.
251. Id. (quoting In re Pommerer, 10 Bankr. 935, 939 (Bankr. D. Minn. 1981)).
252. See supra note 116 and accompanying text.
statutory language.254 Conceding that it is difficult to define where planning ends and hindering creditors begins, the bankruptcy court in Oberst stated that “Congress has decided that the key is the intent of the debtor. . . . This is an uncomfortable test and does not seem equitable; but it is the law.”255 The test as phrased in Oberst, however, also has problems of its own.256

The decision in Johnson, like the Tveten decision, did not answer all the questions raised by the case. In particular, it did not explicitly answer whether the debtor’s future income potential or the dollar value of property converted constitute extrinsic evidence demonstrating intent to hinder, delay, or defraud. Where the legitimate practice of bankruptcy estate planning is at issue, Johnson implies that these facts should not control the outcome.257 Likewise, Tveten also appears to reject this notion, seeing these facts as part of the conversion itself.258

C. Tveten and Johnson in Retrospect

Although Tveten and Johnson are diametrically opposed, the two cases can be reconciled based on the appellate standard of review. Whether the debtor harbored the intent to hinder, delay, or defraud creditors is a question for the finder of fact.259 Because the “clearly

254. Id. at 101. In Oberst, the debtor mortgaged her home thereby removing all of its nonexempt equity. The debtor’s former husband had obtained a judgment of dissolution which required the debtor to pay $16,833.34. Prior to the filing of bankruptcy, the former husband was preparing to execute a writ of execution against the home to collect on the judgment. The bankruptcy court found that the debtor’s conduct in mortgaging the home and spending the proceeds was done in contemplation of bankruptcy and with the intent to hinder, delay or defraud a creditor, namely her former husband. Id. at 101.

255. Id.

256. The court in Oberst states: “If the debtor has a particular creditor or series of creditors in mind and is trying to remove his assets from their reach, this would be grounds to deny the discharge. If the debtor is merely looking to his future wellbeing, the discharge will be granted.” Id. at 101. Yet, this test raises more doubts than it resolves. Cannot a debtor, who is trying to remove assets from his creditor’s reach, also be merely looking to his future wellbeing?

257. Johnson, 80 Bankr. at 963. The court stated:

The gut-level difficulty with the case at bar stems both from the massive amounts of money involved and from Debtor’s status as an affluent physician enjoying sound professional status, excellent current income, and unlimited future earning potential. The vast difference between Debtor’s present circumstances and the financial plight of most consumer and small-business debtors in bankruptcy cannot be denied or ignored. Whether this fact should control or even affect the outcome of an objection to discharge is the question.

Id. at 961. The court ultimately concluded that it should not. See id. at 963.

258. Norwest Bank Nebraska v. Tveten, 848 F.2d 871, 875, 878 (8th Cir. 1988).

259. Johnson, 80 Bankr. at 958.
erroneous” standard of review applies to findings of fact\textsuperscript{260} and because in both cases the bankruptcy courts' findings are not “clearly erroneous,”\textsuperscript{261} the decisions are not inconsistent. Nevertheless, to accurately gauge their value and impact the \textit{Tveten} and \textit{Johnson} decisions must be interpreted in light of the fresh start policy of bankruptcy law; any other analysis would prove myopic.

1. Reconciliation with the Fresh Start Policy

The inevitable confluence of discharge and exemption policies is the fresh start policy. While discharge frees the debtor from the weight of “oppressive indebtedness,” exemptions allow the retention of property to facilitate rehabilitation and protect against impoverishment.\textsuperscript{262} By narrowly construing objections to both discharge and exemptions, the debtor's future economic independence is encouraged. Yet, the value of discharge and exemptions to the individual debtor cannot be assessed strictly in terms of dollars and cents. Discharge also embodies an ineffable emotional and psychological liberation. For some, this freedom may be more valuable than the dollar amount of discharged debts. Similarly, exemptions allow the retention of property to which the debtor may hold strong emotional ties. This is a significant social protection policy in itself.

Suffice it to say, however, that not all debtors are created equal. While an overly generous exemption statute is of little use to debtors with meager resources, debtors with abundant assets are able to reallocate their wealth to maximize exemptions. Fresh start then is by no means a static concept. Some debtors, through no fault of their own, will have a fresher start than others who are less fortunate. This is a fact of life in a land of opportunity. If exemptions are truly necessary to achieving a fresh start, as state legislatures, Congress, and the courts have indicated,\textsuperscript{263} then a debtor's full use of existing exemptions should be limited only to the extent that the full use exceeds the achievement of a fresh start. Where exemptions contain fixed dollar limitations, the extent by which fresh start can be attained through exemptions is known and understood. Where exemptions

\begin{itemize}
\item \textsuperscript{260} \textit{Tveten}, 848 F.2d at 874.
\item \textsuperscript{261} \textit{Cf.} McCormick v. Security State Bank, 822 F.2d 806, 808 (8th Cir. 1987); Lovell v. Mixon, 719 F.2d 1373, 1379 (8th Cir. 1983). As the cases illustrate, bankruptcy judges are divided on this matter. The results of a discussion and straw vote by Midwestern bankruptcy judges on the issue taken at the Nat'l Conference of Bankruptcy Judges in San Diego, October 2-5, 1988, were evenly split. Minnesota Law Journal, Dec. 1988, at 19, col. 1.
\item \textsuperscript{262} \textit{See supra} notes 21-75 and accompanying text.
\item \textsuperscript{263} The debtor's full use of existing exemptions has consistently been encouraged. \textit{See Smiley v. First Nat'l Bank of Belleville (In re Smiley)}, 864 F.2d 562, 567 (7th Cir. 1988) (“[W]e should not prohibit a debtor's full use of exemptions within the limits of the law.”); \textit{see also} \textit{Johnson}, 80 Bankr. at 961.
\end{itemize}
contain no dollar limitation, the fresh start boundary is unclear, but
the debtor's right to a full use of exemptions is not. To invoke the
denial of discharge for a debtor's full use of exemptions undercuts
the fresh start policy by seeking to establish an unrealistic and ideal-
listic equality among debtors. Since debtors entering bankruptcy do
not have equal amounts of indebtedness, why should they emerge
from bankruptcy with an equal amount of assets? Do not debtors
who maximize exemptions fall within the same fresh start concept as
debtors who do not maximize exemptions?

The counter argument, though not without some surface appeal, is
that it is unfair to permit high income debtors an exemption free-for-
all that only serves to shelter wealth through the bankruptcy pro-
cess. This argument hints that exemption provisions should apply
differently to wealthy debtors as compared to not-so-wealthy
debtors.

Exemption laws, created by legislatures and subject to the political
process, do not recognize class or economic distinctions. Should
such distinctions or equality be desired, they must have legislative,
not judicial, beginnings. Penalizing bankruptcy estate planning
does not promote the achievement of fresh start goals where the
debtor's only misconduct is to take advantage of existing law.

There can be no doubt that the conduct in both Tveten and Johnson
was a conscious and avaricious effort to shelter wealth through then
existing state exemption laws. The wage substitute exemptions
claimed in Tveten and Johnson could be easily converted to present
value free from the hands of discharged creditors. Allowing debt-
ors with strong future earning potential to emerge from bankruptcy
with a substantial amount of property intact does not and should not
appeal to one's sense of proportion or equity. That the actions and
results were entirely self-serving is of no consequence to the ultimate
issue presented, namely: Is the practice of bankruptcy estate plan-
ing, regardless of the debtor's future earning potential, the type of
conduct so odious to the fresh start concept that the denial of dis-
charge is warranted? Probably not. Still this begs the question:
When do selfish motives become significant enough to require a de-
ial of discharge?

264. Debtors seeking to shelter wealth through bankruptcy exemptions are not
advancing legitimate exemption goals. See Jackson, supra note 28, at 1444.
265. "This result, however, cannot be laid at the Debtor's feet; it must be laid at
the feet of the Minnesota state legislature." Johnson, 80 Bankr. at 963.
266. Nimmer, supra note 2, at 104.
267. In re Zouhar, 10 Bankr. 154, 157 (Bankr. D.N.M. 1981) ("While a bankrupt is
entitled to adjust his affairs so that some planning of one's exemptions under bank-
rupcy is permitted, a wholesale sheltering of assets which otherwise would go to
creditors is not permissible.").
Despite all the questions surrounding bankruptcy estate planning, it is clear that unlimited state exemptions, although a means, are not the cause of abuse. Rather, abuse is caused by the framework of the bankruptcy exemption statute and the standard used by the courts to test the propriety of conversions to exempt property. It is apparent from either an analytical or ordinary common-sense standpoint that, when a debtor converts property from nonexempt to exempt form, his basic intent is to make it difficult for his creditors to seize that property. The “intent to defraud” standard and badges of fraud approach are cumbersome tools, poorly fashioned for application to the delicate manipulations of bankruptcy estate planning. The problem is exacerbated by the “hinder and delay” standard that denies discharge at the discretion of the bankruptcy court to even the most deserving individuals for engaging in bankruptcy estate planning.

2. The Essence of the Problem

The cases of Tveten and Johnson can be analogized to the story of Icarus and his father Daedalus, who escaped their imprisonment by fashioning artificial wings made of feathers and wax. As the story goes, Icarus, captivated by his own aerial proficiency, flew too near the sun, which melted the wax in his wings and caused him to fall into the sea and drown. As the outcomes in the cases demonstrate, the debtor in Tveten, like Icarus, flew much too high for his fragile wings and crashed. Yet, the debtors in Hanson and Johnson flew just as high with the same delicate device, but avoided disaster by flying in different places and on a cloudy day. The same conduct led to different results solely because of the fortuity of judicial interpretation of the conduct, yet a case should not hinge on the debtor having luckily filed in a favorable court.

In the Eighth Circuit, the bankruptcy courts wield unbridled equitable power in the weighing of these considerations where the debtor has practiced bankruptcy estate planning. By wielding such broad discretionary powers, the traditional inquiry under section 727(a)(2) is transmuted into a procrustean exercise of trimming each case to fit each court’s own sense of equity and proportion. As Judge Arnold’s concurrence in Hanson and dissent in Tveten notes, basic differences between the debtors that were, in his mind, “legally irrelevant”

268. Johnson, 80 Bankr. at 959.
269. See id. at 963
270. The differences by Judge Arnold are:
   (1) Dr. Tveten is a physician and the Hansons are farmers;
   (2) Dr. Tveten attempted to claim exempt status for about $700,000 worth of property, while the Hansons are claiming it for about $31,000 worth of property; and
   (3) the Minnesota exemption statute whose shelter Dr. Tveten sought had
are extremely relevant to the bankruptcy courts when exercising their discretion and equitable powers in applying the per se rule and the badges of fraud analysis to exemption allowances and denials of discharge.271

a. Human Capital

Unlike his bretheren, Judge Arnold recognized that the first difference between Omar Tveten and Hansons is that Tveten is a medical doctor and the Hansons are farmers.272 Dr. Tveten was an individual who had invested a great deal of time and money in himself. Tveten's investment in his own human capital resulted in a high present income as well as a potential for high future earnings.273 The Hansons, on the other hand, were farmers whose prospects for future earnings looked grim. The court recognized, at least impliedly, that based exclusively on potential future earnings, Tveten stood a good chance of achieving a fresh start. The Hansons, possessing doubtful future earning potential, were in a poor position to achieve a successful financial rehabilitation.

b. The Amount of the Claimed Exemption

With the exception of the Hansons' claimed homestead exemption, all of the debtors sought to exempt a form of wage substitute.274 The problem with wage substitute exemptions is that whereas the future value of the property is retained by the debtor only on a transitory basis outside of bankruptcy, once the debtor is discharged, the future value of the property is retained permanently.275 The debtor is free to convert the future value of the property to its present value and the property cannot be reached by the discharged creditors.276 The policy reason for allowing the debtor no dollar limit, while the South Dakota statute exempting the proceeds of the life-insurance policies, S.D. CODIFIED LAWS ANN. § 58-12-4 (1978), is limited to $20,000. 

Hanson, 848 F.2d at 870 (Arnold, J. concurring). But see supra note 163, and accompanying text (South Dakota homestead exemption is also unlimited).

271. Bankruptcy Judge Kishel's thoughtful opinion in Johnson effectively sums up the problems involved in using fraud to measure bankruptcy estate planning abuses. He states:

[T]he use of a "smell" test, while of some utility in the most extreme (presumably to be read "most odious") cases, would be so subject to the pitfalls of subjectivity as to have no paradigmatic value at all. Everyone's nose, after all, is different.

Johnson, 80 Bankr. at 961–62 n.9

272. Tveten, 848 F.2d at 873; Hanson, 848 F.2d at 867.


274. Id.

275. Id. at 103.

276. Id.
to retain these assets, to supplement the debtor's future earnings, is fundamental to bankruptcy estate planning.\textsuperscript{277} But where a debtor is likely to achieve a successful fresh start on the basis of actual future earnings, the reasons for allowing the debtor to exempt this form of property become less compelling.

c. State Exemption Statutes

Because states have the power to force debtors to choose from among several categories of exemptions, bankruptcy estate planning will necessarily involve an intent to "hinder, delay, and defraud" creditors, as currently defined, when a debtor attempts to protect himself, his family, and his future earnings through bankruptcy estate planning. Moreover, state authority to control the exemptions allowed in bankruptcy is likely to result in more categories of exemptions and dollar amounts that do not comport with the federal goal of preserving property that is necessary for ordinary life. The original drafters of the Bankruptcy Code provided for federal exemptions to assure that no debtor was left without property necessary for ordinary life.\textsuperscript{278} At the time of the Code's creation, Congress determined that state exemption statutes did not adequately fulfill this goal.\textsuperscript{279} The federal exemptions generally include specific dollar amounts rather than exemptions based solely on property type. This type of exemption structure assures that bankruptcy estate planning can be utilized only up to the amount of the conferred exemption. The debtor does not have to convert property or transfer assets in order to claim the property as exempt. The debtor only needs to include the property claimed as exempt within the shield of the specific dollar amount allowed under the statute.\textsuperscript{280} Hence, it is not the standard of fraud that has made bankruptcy estate planning a troublesome issue, but the opt-out compromise, as well as generous exemption statutes limited only by the elusive concept of reasonableness, such as those previously available under Minnesota law.\textsuperscript{281} Still, the courts demand that the exemption tail wag the discharge dog.

As illustrated by \textit{Tveten}, the standard under section 727(a)(2) has evolved into an equitable balancing test examining two factors when

\begin{itemize}
  \item\textsuperscript{277} See Jackson, supra note 28, at 1438.
  \item\textsuperscript{278} 11 U.S.C. § 522 (1982 & Supp. IV 1986); 4 Collier on Bankruptcy (MB) ¶ 522.08 (15th ed. 1988); Eisenberg, supra note 90, at 995.
  \item\textsuperscript{279} Eisenberg, supra note 90, at 995; see Nimmer, supra note 2, at 995.
\end{itemize}
reviewing the debtor’s bankruptcy estate planning: (1) the future earning potential of the debtor; and (2) the amount of property claimed as exempt. Under this test, a debtor possessing potentially high future earning who attempts to supplement future earnings by claiming large property exemptions is suspect and considered a poor candidate for discharge. This test strays from the express language of the Bankruptcy Code toward a misplaced reliance on the bankruptcy court’s traditional equitable powers. To this extent, the Eighth Circuit Court of Appeals decision in *Tveten* is directly contrary to the United States Supreme Court’s mandate in *Norwest Bank Worthington v. Ahlers* that “whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code.”

The salutary effect of this standard under section 727(a)(2) is questionable at best. The court of appeals balancing test is “subject to the pitfalls of subjectivity.” The distinction between lawful and unlawful conversions will ultimately rest on whether the particular bankruptcy court holds that ensuring a debtor’s full use of exemptions is paramount to protecting creditor’s rights, or vice versa. The weighing of these competing interests is a perennial debate in the bankruptcy courts. While the debate rages on, debtors preparing for bankruptcy cannot accurately determine the legality of any proposed purchase of exempt property. They sit under the sword of Damocles. The *Tveten* holding endorses a broad grant of discretionary, equitable powers to the bankruptcy courts of the Eighth Circuit by abandoning a straight forward application of a controlling statute in favor of a colloquial phrase better left to govern matters of animal husbandry.

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283. *Id.* at 969.
284. *Johnson*, 80 Bankr. at 961 n.9.
286. *Id.* at 149.
287. *See Id.* at 961 n.9. In discussing this test Bankruptcy Court Judge Kishel stated:

This test is popularly phrased via the fine, homely folk adage of “The pig gets fattened, but the hog gets slaughtered.” . . . (using the variant: “There is a principal of too much; phrased colloquially, when a pig becomes a hog it is slaughtered.”). Use of this metaphor to structure a standard under section 727(a)(2)(A) would produce problems, but it would be at least marginally more defensible than the other colloquialism suggested by Plaintiff’s counsel [the “smell” test]. . . . Animal husbandry at least furnishes weight and age tests to divide “pigs” from “hogs.” . . . Everyone’s nose, after all, is different.

*Id.*
IV. Suggestions and Conclusions

Bankruptcy law, like any law, encourages planned efforts to avoid its mandates.\(^{288}\) An immediate step that the courts should take is the determination of the proper standard of proof for an objection to discharge. Considering the severity represented by a denial of discharge, a standard higher than the civil "preponderance of the evidence" standard should be used.\(^{289}\) Beyond this, as Johnson points out, judicial alternatives are limited.\(^{290}\) In contrast, legislative alternatives remain a possible and probably more effective solution.

Bankruptcy estate planning provides Congress an opportunity to establish a definite federal rule permitting or proscribing such conduct. This could be done in a variety of ways. Bankruptcy estate planning conversions are analogous to preferential transfers to creditors.\(^{291}\) These conversions, like preferential transfers, lessen the overall pool of assets available to all creditors.\(^{292}\) Accordingly, a rule similar to the preference rule could be enacted by Congress which would make voidable conversions to exempt property which occur within a certain period before filing bankruptcy. Although it would limit eve of bankruptcy conversions, this approach would have the unsavory effect of conditioning the availability of an exemption for certain property on the debtor’s having owned it for a minimum period of time.\(^{293}\) Alternatively, the opt-out provisions contained in section 522 could be repealed to limit debtors to the federal exemptions; exemptions which presumably advance social and fresh start policies. This would make exemptions uniform, but it would undermine state prerogatives or ignore the needs that may be peculiar to debtors within a certain state. Finally, exemption provisions of section 522 could be replaced entirely by a provision allowing the

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\(^{288}\) Eisenberg, supra note 90, at 991.

\(^{289}\) See In re Obersi, 91 Bankr. 91, 100 (Bankr. C.D. Cal. 1988) (discharge is to be construed liberally in favor of the debtor requiring more than a mere preponderance of the evidence to deny discharge); In re Booth, 70 Bankr. 391, 394 (Bankr. D. Colo. 1987) ("the severity of an attack on dischargeability under section 727 warrants the application of the clear and convincing standard in establishing proof of nondischargeability"); In re Cohen, 47 Bankr. 871, 874 (Bankr. S.D. Fla. 1985) ("the burden must be met with evidence that is clear and convincing"); In re Hargis, 44 Bankr. 225, 228 (Bankr. W.D. Ky. 1984) ("a charge under section 727 must be sustained by persuasive and convincing evidence"); In re Butler, 38 Bankr. 884, 888 (Bankr. D. Kan. 1984) ("the inference of actual intent to hinder, delay or defraud may be drawn from convincing evidence").

\(^{290}\) Johnson, 80 Bankr. at 962.

\(^{291}\) See 11 U.S.C. § 547(b) (1982 & Supp. IV 1986). Under § 547(b) certain transfers made by the debtor may be avoided by the trustee for the benefit of the estate. See Eisenberg, supra note 90, at 993-95.

\(^{292}\) Eisenberg, supra note 90, at 994.

\(^{293}\) Harris, A Reply to Theodore Eisenberg’s Bankruptcy Law in Perspective, 30 UCLA L. Rev. 92, 941 (1982).
debtor exempt property up to a set dollar limitation. The debtor would be allowed to choose which property and in what amount he wanted exempt. The obvious problem with this approach is that exemption choices will be influenced by factors apart from the social and economic concerns that have been the traditional focus of exemption legislation.

As the number of bankruptcy filings increase, so too will instances of bankruptcy estate planning. In response, courts have a responsibility to apply existing law before creating new law. To the extent that Tveten represents a broad grant of equitable power, the precedential value should, in light of the express provisions of section 727 (a)(2)(A), be limited by the United States Supreme Court’s statement in Ahlers. The questions raised by Tveten, Hanson, and Johnson remain. Without a clear standard against which to evaluate the bankruptcy estate planning, debtors and creditors alike must endure the climate of uneasiness and confusion. The articulation and application of a coherent standard consistent with section 727(a) will facilitate fresh start as well as exemption policies without sacrificing one at the expense of the other.

Bryan J. Leary
Thomas G. Wallrich


295. See supra note 271.